



**Arkansas IOLTA Foundation Guidebook
For
Attorneys and Financial Institutions**

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INTEREST ON LAWYERS' TRUST ACCOUNTS (IOLTA)

INTRODUCTION

The Arkansas Supreme Court created the Arkansas IOLTA program in 1984 to provide funds for legal aid to the poor, for student loans and scholarships, and for projects that improve the administration of justice. The Arkansas IOLTA Foundation, Inc. administers the program. Under Rule 1.15 of the Arkansas Model Rules of Professional Conduct, lawyers who receive, maintain or disburse client trust funds are required to maintain those funds in interest-bearing accounts, either for the benefit of the individual client or the Arkansas IOLTA Foundation.

Lawyers routinely receive client funds (proceeds from settlements, filing fees, retainers, etc.) which they place in a bank account for future use. Since the funds are being held for the benefit of the client, lawyers must place these funds in an account separate from their general operating account.

Lawyers should establish separate, interest-bearing accounts for individual client's funds where the sum is large enough or when the time of the deposit is of sufficient duration to justify the costs of opening, closing and administering the account. The individual client receives the interest from the separate account and assumes the tax liability for the interest.

However, if the funds are small or short-term, it is often impractical for the attorney and bank to establish separate interest-bearing accounts that would result in any interest accruing to individual clients. In this circumstance, the lawyer places the client's funds in the lawyer's or law firm's multi-client IOLTA account until distribution. These clients do not receive the interest from this pooled IOLTA account; instead, banks remit the interest directly to the Foundation. Under the Rule it is up to the lawyer to determine whether a client's trust funds will be placed in a separate account for the benefit of the individual client or in the lawyer's multi-client IOLTA account.

Although financial institutions are not required to participate in the IOLTA program, over 160 financial institutions in Arkansas offer IOLTA accounts to their attorney customers and are on the approved list maintained by the Office of Professional Conduct.

The Internal Revenue Service made a final ruling that the Arkansas IOLTA Foundation, Inc. is a 501(c)(3) nonprofit corporation and a 509(a)(1) publicly supported foundation. The Board of Governors of the Federal Reserve System, the FDIC and the Federal Home Loan Bank Board approve of the Arkansas IOLTA program. Copies of these documents are available from the IOLTA office.

This Guidebook is designed to provide information about the Arkansas IOLTA program and to assist participating financial institutions and lawyers in establishing and maintaining IOLTA accounts. Please call the IOLTA office if we can be of assistance to you as you administer IOLTA accounts at your institution or in your law firm. Our telephone number is (501) 682-9421.

DEFINITION OF IOLTA ACCOUNT

An IOLTA (Interest on Lawyers' Trust Accounts) account is an interest-bearing account that an attorney or law firm maintains for commingled client trust funds that are nominal in amount or held for a short term. Per Rule 1.15, the funds in the account must be subject to withdrawal "upon request and without delay." The account is issued in the name of the attorney or law firm, is owned by the attorney or law firm, and is referred to as the Arkansas IOLTA account of (name of lawyer or law firm). All interest earned on the IOLTA account (less *applicable* service charges and fees) is remitted to the Arkansas IOLTA Foundation, Inc.

ATTORNEY PARTICIPATION AND COMPLIANCE

On October 17, 1994, the Supreme Court of Arkansas changed the nature of the IOLTA program from voluntary to mandatory effective April 17, 1995. All Arkansas lawyers and law firms receiving short-term or nominal client funds must place those funds in interest-bearing trust accounts.

Rule 1.15 requires lawyers to notify their clients of their IOLTA account by posting a notice in a conspicuous place in their law offices. Contact the Foundation's staff if you need a copy for your law office.

The Rule requires all licensed Arkansas lawyers to certify their compliance annually to the Arkansas Supreme Court at the time of annual renewal of the lawyer's license. If a lawyer or law firm has not complied with Rule 1.15, the lawyer will be referred to the Arkansas Supreme Court Committee on Professional Conduct for investigation.

If a lawyer or law firm closes an IOLTA account, the lawyer or law firm should notify the Foundation's staff. If a lawyer's IOLTA status changes during the year, the lawyer should contact the Foundation's office in order to complete a new IOLTA Compliance Statement.

A lawyer or law firm should periodically review its IOLTA account to determine whether client funds should be moved due to changed circumstances.

EXEMPTION FROM PARTICIPATION

Under Rule 1.15 a lawyer may be exempt from participating in the IOLTA program. Certain automatic exemptions are found in the IOLTA Compliance Statement issued by the Clerk of the Arkansas Supreme Court. In addition, if a lawyer's IOLTA account routinely carries a low balance or if service charges equal or exceed the interest generated, the lawyer may be exempt from maintaining the account if the Foundation's Board of Directors so determines. The latter exemption is for no more than two (2) years; the lawyer must then re-establish an IOLTA account for short-term or nominal client trust funds.

TAX IDENTIFICATION NUMBER

The tax identification number for all IOLTA accounts is the Foundation's TIN: #71-0611874. The IRS matches the TIN with the payee; the tax identification number will not match the name on the account unless the account name includes "the Arkansas IOLTA account of (name of lawyer or law firm)." The Foundation is the beneficiary of the interest for reporting purposes.

IRS REPORTING NOT REQUIRED

IOLTA accounts are exempt from any backup withholding tax. Financial institutions DO NOT need to send out a request for taxpayer identification number, IRS Form W-9. If the bank's procedures require the receipt of a W-9 form, it should list the Foundation's TIN and we will sign it.

Neither the financial institution nor the law firm is required to report interest earned on the IOLTA account. Financial institutions should dispense with the issuance of IRS Form 1099. If the financial institution's data processing system automatically issues a Form 1099, the form should indicate the name of the attorney or law firm and the tax ID of the Foundation and should be sent to the Foundation.

Interest on IOLTA accounts is not includable in the gross income of either the clients or the lawyers. (IRS Rev. Rul. 81-209)

SERVICE CHARGES AND HANDLING FEES

The majority of participating financial institutions in Arkansas waive fees on IOLTA accounts. However, the Arkansas IOLTA Foundation, Inc. will cover customary, routine account maintenance charges assessed against IOLTA accounts. According to the Rule, these fees may not exceed those charged to non-attorney customers " . . . on accounts of the same class within the same

institution." Such routine fees include a monthly maintenance fee, per check/per deposit charge, and a "reasonable" IOLTA remittance fee to defray the depository institution's costs attributable to calculating and remitting the interest on the account to the Foundation. We encourage financial institutions to discuss IOLTA remittance fees with the Foundation.

Fees for wire transfer, insufficient funds, bad checks, stop payment, account reconciliation, negative collected balances, and check printing are not considered customary account maintenance charges and are not covered by the Arkansas IOLTA Foundation, Inc. Such non-routine fees must be brought to the attention of the lawyer or law firm.

The Foundation may define reasonable service charges and handling fees in light of the prevailing financial environment and may remove a bank from the approved list of financial institutions authorized to offer attorney IOLTA accounts.

The financial institution should deduct applicable service charges and handling fees for IOLTA accounts solely from the interest earned. The principal of the account should never be used to offset the service charges or handling fees imposed on an IOLTA account. Since these accounts contain client funds held in trust by attorneys, any invasion of the principal would be improper.

"Negative" interest earnings are strictly prohibited on IOLTA accounts. This would result from service charges that exceed interest earned and would constitute an invasion of principal. "Negative netting"—collecting these negative charges from the interest earned by other IOLTA accounts—is also prohibited. This practice would constitute payment of fees of one account with earnings from another account without the account holder's consent. Service charges may only be imposed to the extent of interest earned on an individual account. For example, if an IOLTA account earns 50 cents in interest for a given month but the financial institution's normal monthly maintenance fee is \$1, only 50 cents may be charged. The excess service charge amount is waived by the financial institution and net interest paid is reported as "zero" on the IOLTA interest remittance report form.

FDIC INSURANCE

An FDIC Advisory Opinion, published in September, 1992, states that funds which are deposited into a law firm's trust account are the property of the individual clients represented and will be insured up to the \$100,000 aggregate amount per client, regardless of the total dollars in the account or any other deposits/accounts the law firm may have within that institution. **However, the lawyer or law firm must have records showing the principal amounts attributable to individual clients.** Following is an excerpt from that opinion:

“ . . . The FDIC insurance regulations state that the deposit account records of an insured depository institution must disclose the existence of any fiduciary relationship before any claim for deposit insurance based on that relationship will be recognized. 12 C.F.R. Section 330.4(b)(1). If the deposit account records of the insured depository institution do disclose the existence of a fiduciary relationship, the details of the relationship and the interests of the other parties in the account can then be determined either from the deposit account records of the insured depository institution or from the records of the fiduciary, the nominal depositor (or some person or entity whom the fiduciary has engaged to perform that task). 12 C.F.R. Section 330.4(b)(2).

An IOLTA account must therefore disclose that the funds in the account are held by the nominal account holder (the lawyer) on the behalf of others. If this disclosure requirement is met, the FDIC will then be able to ascertain the interests of other parties in the IOLTA account from the records of the insured depository institution or from the records of the lawyer (or from some person or entity whom the lawyer has engaged to perform that task). If this record keeping requirement is satisfied, **funds attributable to each client will be insured to the client in whatever right and capacity that the client owns those funds.** For example, if an IOLTA account contains funds that belong to an individual, they will be insured up to \$100,000 as individual funds. These funds will be aggregated and insured to the statutory limit, however, with any other funds which the client may hold individually at the same insured depository institution. The accrued interest which is attributable to the tax-exempt entity will also be recognized as a separately insured interest if the disclosure and record keeping requirements are met.”

SETTING UP AN IOLTA ACCOUNT

IOLTA accounts must be interest-bearing checking accounts that provide for the lawyer or law firm to write a sufficient number of checks without penalty. Two (2) forms are used to set up an IOLTA account. The attorney completes the Notice to Financial Institution to Establish An IOLTA Account form. It is important to use the Foundation’s tax ID number as it appears on the form. The financial institution completes the Confirmation of IOLTA Account form. Either the attorney or the financial institution should fax both completed forms to the Foundation, as that is the only way we know a new account has been established. The financial institution usually keeps the originals, but there is no requirement that they do so. Forms may be obtained from the IOLTA office or downloaded from <http://courts.state.ar.us>. Many financial institutions have copies of these forms on hand.

Please list the name on the signature card as “Arkansas IOLTA Account of (name of lawyer or law firm).” Use the Foundation’s TIN: 71-0611874.

Rule 1.15 provides that an attorney may deposit his or her own funds into the account to the extent required for banking purposes, but not to exceed \$500. These funds must be clearly identified in the lawyer's or law firm's records of the IOLTA account.

OVERDRAFT NOTIFICATION

Participating financial institutions must report overdrafts on IOLTA trust accounts to the Office of Professional Conduct (even if the insufficient instrument is honored). This should be done simultaneously with the notice of overdraft to the lawyer or law firm.

Rule 1.15 stipulates that notice of a dishonored instrument should be identical to that normally sent to a depositor and should include a copy of the check if that is the financial institution's customary practice. The Rule also stipulates that insufficient instruments that are honored by the financial institution should contain the following information:

- 1.) identify the financial institution;
- 2.) identify the lawyer or law firm;
- 3.) show the account number;
- 4.) show the date of presentation for payment;
- 5.) show the date paid; and
- 6.) the amount of the overdraft.

Overdraft notices should be mailed to the Office of Professional Conduct, 110 Justice Bldg., 625 Marshall Street, Little Rock, AR 72201, telephone (800) 506-6631 or (501) 376-0313 and fax (501) 376-3438.

REPORTING ON ACCOUNTS AND PAYING THE INTEREST

The Foundation initiates a fax Remittance Report to each participating financial institution on the last working day of each month requesting information on interest earned for that month. The Remittance Report contains all the account numbers and names of lawyers or law firms with IOLTA accounts at that financial institution. The financial institution should complete the report and fax it back to the Foundation within five (5) business days. Corrections to the form may be made directly on the form (closed accounts, new accounts, and any additional information the financial institution would like for the Foundation to have).

If a financial institution elects to submit an institutionally-generated report, the format should follow a sort order:

- 1.) By account number;

- 2.) Customer name;
- 3.) Average daily account balance;
- 4.) Interest rate paid on the account;
- 5.) Interest earned for the period;
- 6.) Service charges (if applicable) deducted from the interest; and
- 7.) Net amount of interest remitted.

The participating financial institution is responsible for monthly remittance of IOLTA funds. The interest funds may be remitted via the ACH (Automated Clearinghouse) method or by the check method. The financial institution selects the method by completing the Confirmation of IOLTA Account form and faxing this form to the Foundation.

Automated Clearinghouse (ACH) Method:

To simplify processing IOLTA accounts the Foundation will initiate the transfer of interest via an ACH debit. This method is available to all banks that waive minimum balance requirements and remittance fees on IOLTA accounts. The Foundation debits the interest from each account once a month, normally between the 10th and the 15th of the month.

The financial institution may choose to establish **one in-house account** in which the financial institution places all IOLTA interest earned on each IOLTA account for the month. The Foundation then debits the in-house account, again normally between the 10th and the 15th of the month.

To utilize this method all the financial institution need do is complete and fax back the Remittance Report on a monthly basis.

Check Method:

The financial institution may remit monthly by:

- 1.) Sending one check for interest earned on all IOLTA accounts along with a copy of the Remittance Report.
- 2.) Sending a separate check for interest earned on each IOLTA account along with a copy of the Remittance Report.

A financial institution should transmit to the lawyer or law firm at the same time a report or statement showing the amount of interest paid to the Foundation, the rate of interest applied, the fees assessed, and the average account balance for the period for which the report is made. An entry on the lawyer's or law firm's bank statement meets this requirement. **It is the lawyer or law firm's obligation to reconcile the IOLTA account financial institution statement on a monthly basis to ascertain that the interest is being transferred from the**

financial institution to the Foundation. Rule 1.15(a)(4) requires a lawyer to utilize generally accepted accounting practices with regard to trust accounts.

RATE OF INTEREST

The rate of interest payable on any IOLTA account shall not be less than the rate paid by the depository institution on Negotiable Order of Withdrawal (NOW) or Super Negotiable Order of Withdrawal accounts at that institution as permitted under 12 U.S.C. Section 1832(a) or any successor provision.

REFUNDS

The Foundation will issue refunds when interest has been remitted in error. Refunds will be made to the financial institution upon notification and proper documentation.

AN EXCELLENT OPPORTUNITY FOR FINANCIAL INSTITUTIONS

IOLTA doesn't just aid the justice system in Arkansas; the concept provides very favorable exposure for participating financial institutions as well.

- The Foundation publishes an annual IOLTA Bank Honor Roll in The Arkansas Lawyer magazine, a publication of the Arkansas Bar Association. The Honor Roll recognizes participating banks by tier according to interest rates paid and waiver of fees and service charges. The magazine reaches an audience of over 5,000 attorneys and law firms.
- You should also reflect IOLTA contributions in your banking information brochures, newsletters, and annual reports to shareholders. By doing this, you let investors and customers know that your financial institution is playing an active role to strengthen the judicial system and to help fund worthwhile law-related programs in your community.
- Promoting IOLTA is good business for your institution. Since an IOLTA account is a multi-client pooled account, average balances can often run significantly higher than similar deposit accounts, and as a class of accounts, offer greater potential for low-cost deposits. Further, attorneys are an excellent source for cross-selling banking services, such as consumer and business loans, other deposit accounts, mortgage services, and escrow services.

- If your financial institution wants to participate in IOLTA but has no attorney trust accounts at the present time, just give the Foundation staff a call. We will list your bank in all our publications as a participating IOLTA institution.
- Finally, the Arkansas IOLTA Foundation Board of Directors has adopted a policy of reinvesting IOLTA funds only in financial institutions that offer IOLTA accounts.

CONCLUSION

These guidelines are established by the Board of the Arkansas IOLTA Foundation, Inc. for the Arkansas IOLTA program. If your financial institution wishes to modify any of the procedures described herein, please contact the Foundation's staff to discuss your individual needs and/or concerns. We strive to accommodate the needs of financial institutions offering IOLTA accounts to their lawyer customers.

The Arkansas IOLTA Foundation, Inc. is very grateful to its participating lawyers and financial institutions. We are especially grateful to those financial institutions that waive fees and charges. The Foundation and Legal Aid clients are extremely fortunate to have the dedication of thousands of Arkansas attorneys to the IOLTA program. These attorneys understand Legal Aid's vital role in the provision of equal access to justice. Attorney customers throughout the state frequently inquire about specific practices of a financial institution with regard to IOLTA accounts. It is our practice in those instances to offer information and any helpful historical data relating to fees imposed, interest rates, and IOLTA banking procedures.

We pledge to work with lawyers and financial institutions to make Arkansas' IOLTA program a success. Do not hesitate to raise any concerns you have with our staff at any time.

APPENDIX

1. Rule 1.15 of the Arkansas Model Rules of Professional Conduct.
2. Approved Trust Account Depositories Listing.
3. Form/Notice to Financial Institution to Establish An IOLTA Account.
4. Form/Confirmation of IOLTA Account.
5. Form/IOLTA Compliance Statement.
6. Section 28 Procedures on Overdrafts.